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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 577

FLORENCE H. EHRMAN, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

CLARA HELLMAN HELLER, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

FRANCES J. HELLMAN AND WELLS FARGO BANK & UNION TRUST CO., TRUSTEES UNDER THE LAST WILL AND TESTAMENT OF I. W. HELLMAN, JR., DECEASED, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 24–48) is reported in 41 B. T. A. 652. The

opinion of the Circuit Court of Appeals (R. 156-163) is reported in 120 F. (2d) 607.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 6, 1941 (R. 164). The petition for a writ of certiorari was filed September 2, 1941. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether gains realized by the petitioners from the subdivision of property owned by them and the sale of lots constituted ordinary income or capital gains under Section 117 (b) of the Revenue Act of 1934.

STATUTE INVOLVED

Revenue Act of 1934, 48 Stat. 680:

> SEC. 117. CAPITAL GAINS AND LOSSES.
>
> (a) *General Rule.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net income:
>
> * * * * *
>
> 30 per centum if the capital asset has been held for more than 10 years.
>
> (b) *Definition of Capital Assets.*—For the purposes of this title, "capital assets" means property held by the taxpayer

(whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business (U. S. C., Title 26, Sec. 101).

STATEMENT

The facts as found by the Board of Tax Appeals (R. 25–40) may be summarized as follows:

I. W. Hellman, Sr., was a banker. At his death in 1920 he left a considerable estate which included a large number of tracts of land, both improved and unimproved. This land included several ranch properties, one of which was Repetto Ranch, containing 1,569.93 acres and located about five miles east of the City Hall of Los Angeles, but outside the city limits. Repetto had been acquired by Hellman, Sr., between 1870 and 1880. It was used first for grazing and later, until 1929, for farming and horticulture (R. 26–27).

Upon the death of Hellman, Sr., the residue of his estate, including Repetto, passed in equal parts to his children. Two of the children and the trustee under the will of the third child are the petitioners here (R. 27).

No particular effort was made to sell Repetto prior to 1929. Offers were received and (except for two sales, totalling 8.5 acres) were rejected

by the petitioners, who were opposed to a subdivision project and wished to sell outright, either for cash or substantial cash and security for the balance. However, in 1929 about 800 acres of Repetto, constituting practically all of its level land, were sold to Ransom Corporation, which proposed to subdivide the land and sell it. The total consideration for the sale was $4,052,000, with a down payment of $250,000 cash, and the balance payable with interest over a period of approximately ten years. Title was conveyed to a bank, as trustee, under a declaration of trust (R. 27–29, 44, 72).

Ransom proceeded to develop a portion of the land, but in 1931 and 1932 became involved in difficulties. After negotiations the parties on May 16, 1932, entered into a modification of the declaration of trust, whereby all of the land except approximately 273 acres was released and the total purchase price reduced. Thereafter Ransom continued its efforts, but in a short time defaulted under the amended agreement, and on December 2, 1932, gave notice that it could no longer proceed. On July 31, 1933, the petitioners demanded sale and on February 13, 1934, purchased the property at trustee's sale, and deed was delivered to them on May 30, 1934 (R. 29–30).

The property so reacquired by the petitioners had been subdivided into lots, some of which had been deeded to purchasers and some of which were

under contracts of sale. The uncompleted contracts were acquired by the petitioners, as well as certain obligations, such as improvement and maintenance of the property and street and drainage district assessments. Prior to the trustee's sale petitioners' agent, Keller, investigated the situation at their request and advised that they carry on with the subdivision, first reducing the price of the lots to meet the market at that time. The Hamilton Sales Corporation was thereupon employed as agent of petitioners to carry on the work of the subdivision, and Hamilton started operations in November 1933, prior to the foreclosure.[1]

The first thing done was to restore to acreage parts of the land on which not many lots had been sold or contracted for sale. About 46 acres were so restored, and at about the same time, on November 9, 1933, a new tract of approximately 40 acres was opened by the petitioners for subdivision purposes, in order to centralize the entire subdivision and bring it closer to the business section (R. 30–32).

Two additional tracts were later added to the subdivision, one of 34.8 acres in 1937, and one of 64.8 acres in 1938, and subdivided by the peti-

[1] The contract between petitioners and Hamilton was entered into on February 19, 1934. It provided, in general, that Hamilton through its own sales organization was, for a commission, to sell the subdivided lots, subject to the direction of petitioners (R. 32–34; Pet. 6).

tioners. Shortly after Hamilton took over, the petitioners built and paid for five houses on the subdivision, for the purpose of promoting sales. Hamilton developed an active sales organization, including as many as 200 salesmen. Petitioners maintained and improved the subdivided property at their own cost, and contracted for public utility facilities for the subdivision as well as for improvement and maintenance, expending substantial sums for all these purposes (R. 34–35, 39).

Lot contracts and sales under the subdivision program were as follows (R. 36):

	Number of contracts, lots	Total sale price	Total payments made on contracts
1934	120	$161,679.87	$59,625.44
1935	186	230,170.00	105,276.70
1936	264	296,029.00	139,379.99
1937	258	342,565.00	230,465.88
1938	234	285,446.43	226,346.62

The petitioners returned the resulting income as capital gains and the Commissioner assessed deficiencies (R. 40, 20–22). The Board of Tax Appeals sustained his determination (R. 49–51). It found that the petitioners could have sold the whole ranch for a fair price and that they subdivided simply to obtain a better price (R. 44–45) and that the continuity and frequency of the sales showed that the property was held for a business sale (R. 47). The circuit court of appeals affirmed (R. 164).

ARGUMENT

1. Petitioners' argument seems to be that so-called "investment property" must retain that status and cannot become the subject of "business." But, even if property used for grazing and agriculture falls within petitioners' category of "investment property", section 117 (b) excludes from the capital gains provisions "property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business." However acquired, the property after the inauguration of the subdivision program was obviously held for sale to customers in the ordinary course of that program. The assertion (Pet. 22) that subdivision was the only available means of sale is similarly irrelevant, and is in any event contradicted by the finding of the Board of Tax Appeals (R. 43–46).[2]

2. This is the fourth time that the court below has reached the same result upon parallel sets of facts. *Welch* v. *Solomon,* 99 F. (2d) 41 (C. C. A. 9); *Richards* v. *Commissioner,* 81 F. (2d) 369 (C. C. A. 9); *Commissioner* v. *Boeing,* 106 F. (2d) 305, certiorari denied, 308 U. S. 619. However, conflict is urged between the holding below and the

[2] The 1934 amendment, mentioned by petitioners (Pet. 23), adding the qualification that the sales must be "to customers" in the "ordinary" course of business, is irrelevant to sales such as these, and was designed only to include stock speculators within section 117. See H. Rpt. No. 1385, 73d Cong., 2d Sess., p. 22.

decisions in *Phipps* v. *Commissioner,* 54 F. (2d) 469 (C. C. A. 2), and *Pope* v. *Commissioner,* 77 F. (2d) 599 (C. C. A. 6). As shown by petitioners' quotations from *Phipps* v. *Commissioner* (Pet. 20), both the Second Circuit and the court below view the result as turning upon the continuity and the frequency of the sales, and the difference in result simply reflects the difference in the factual situations presented. In *Pope* v. *Commissioner, supra,* the court assumed that a real estate business was being conducted and merely held that the taxpayer, who was a stockholder and an inactive officer, was not engaged in the business of the corporation. The petition for a writ of certiorari in the *Boeing* case, which also claimed a conflict with the *Phipps* and *Pope* cases, was denied. While the asserted conflict did not receive the emphasis present counsel would have given it (Pet. 22), it was distinctly asserted (No. 511, October Term, 1939, Pet., pp. 11, 28) and was specifically answered in the brief in opposition (p. 11).

3. *Higgins* v. *Commissioner,* 312 U. S. 212, dealt with the question whether personal investment expenses were deductible as business expenses, and *Morrissey* v. *Commissioner,* 296 U. S. 344, with the question whether a trust was engaged in business. Apart from the dissimilarity in the facts of the cases, this Court has already recognized that the content of the definitions of doing business

necessarily varies in these diverse inquiries. *Higgins* v. *Commissioner, supra,* 217.

CONCLUSION

The decision below is correct and there is no conflict. It is, therefore, respectfully submitted that the petition should be denied.

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